DEPARTMENT OF STATE REVENUE

04-20130306.LOF

Letter of Findings Number: 04-20130306
Sales and Use Tax
For Tax Years 2010 and 2011

NOTICE: Under IC § 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of the document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

I. Sales and Use Tax – Computer Based Information Technologies.

Authority: IC § 6-2.5-1-27; IC § 6-2.5-3-2; IC § 6-8.1-5-1; Indiana Dep't of State Revenue v. Kimball Int'l Inc., 520 N.E.2d 454 (Ind. Ct. App. 1988); General Motors Corp. v. Indiana Dep't of State Revenue, 578 N.E.2d 399 (Ind. Tax Ct. 1991) aff'd 599 N.E.2d 588 (Ind. 1992); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Sales Tax Information Bulletin 8 (May 2002); Sales Tax Information Bulletin 8 (November 2011).

Taxpayer protests the assessment of use tax on web-based information platforms and computer software programs.

II. Sales and Use Tax – GPS Units.

Authority: IC § 6-2.5-5-8; IC § 6-8.1-5-1; Brambles Industries, Inc. v. Indiana Dep't of State Revenue, 892 N.E.2d 1287 (Ind. Tax Ct. 2008); Miles, Inc. v. Indiana Dep't of State Revenue, 659 N.E. 2d 1158 (Ind. Tax Ct. 1995); 45 IAC 2.2-5-15.

Taxpayer protests the assessment of use tax on global positioning system ("GPS") units that were installed onto vehicles that Taxpayer sold.

STATEMENT OF FACTS

Taxpayer operates a new and used car dealership in Indiana, with a service and body shop department. The Indiana Department of Revenue ("Department") conducted income, withholding, tire fee, auto rental excise tax, and sales and use tax audits of Taxpayer for the years 2010 and 2011. There were no adjustments pursuant to the income tax, withholding tax, tire fee, or auto rental excise tax audits. The sales and use tax audit resulted in the assessment of additional use tax, penalty and interest. Taxpayer agreed to some of the use tax issues and remitted partial payment. Taxpayer protested the use tax assessments on several computer based information technologies, as well as GPS units that it installed in automobiles it sold.

An administrative hearing was conducted during which Taxpayer's representative explained the basis for the protest. Taxpayer submitted some additional documentation at the hearing. This Letter of Findings results. Additional facts will be provided as necessary.

ISSUES

I. Sales and Use Tax – Computer Based Information Technologies.

DISCUSSION

Taxpayer purchased several different computer based information technologies, such as internet-based information platforms and computer software programs for different business functions, without paying sales tax or self-assessing use tax. The Department's audit determined that use tax should be imposed on those items. Taxpayer maintains that the software and web-based platforms were exempt from sales or use tax.

The Department notes that all tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007). In applying any tax exemption, the general rule is that "tax exemptions are strictly construed in favor of taxation and against the exemption." Indiana Dept. of State Revenue v. Kimball Int'l Inc., 520 N.E.2d 454, 456 (Ind. Ct. App. 1988). The taxpayer claiming exemption has the burden of showing the terms of the exemption statute are met. General Motors Corp. v. Indiana Dept. of State Revenue, 578 N.E.2d 399, 404 (Ind. Tax Ct. 1991) aff'd 599 N.E.2d 588 (Ind. 1992) (Internal citations omitted). Additionally "[e]xemption statutes are strictly construed because an exemption releases property from the obligation of bearing its fair share of the cost of government." Id.

Pursuant to IC § 6-2.5-2-1, a sales tax, known as state gross retail tax, is imposed on retail transactions made in Indiana unless a valid exemption is applicable. Retail transactions involve the transfer of tangible personal property. IC § 6-2.5-3-2(a). A complementary excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction. IC § 6-2.5-3-2.

Specifically, IC § 6-2.5-2-1 provides as follows:

(a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana.

(b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to

the consideration in the transaction. The retail merchant shall collect the tax as agent for the state.

IC § 6-2.5-3-2(a) provides for the complementary use tax:

An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

In this case, the audit found that Taxpayer had made purchases which were subject to sales tax but failed to pay that tax. Therefore, the audit assessed the complementary use tax.

Computer software and updates are considered tangible personal property which is taxable under IC § 6-2.5-1-1. IC § 6-2.5-1-27 provides that "tangible personal property" would also include "prewritten computer software." Sales Tax Information Bulletin 8 (May 2002), 25 Ind. Reg. 3934, provides in part:

As a general rule, transactions involving computer software are not subject to Indiana Sales or Use Tax provided the software is in the form of a custom program specifically designed for the purchaser. Pre-written programs, not specifically designed for one purchaser, developed by the seller for sale or lease on the general market in the form of tangible personal property and sold or leased in the form of tangible personal property are subject to tax irrespective of the fact that the program may require some modification for a purchaser's particular computer. Pre-written or canned computer programs are taxable because the intellectual property contained in the canned program is no different than the intellectual property in a videotape or a textbook.

Furthermore, Sales Tax Information Bulletin 8 (May 2002), 25 Ind. Reg. 3934, provided that:

Pre-written programs, not specifically designed for one purchaser, developed by the seller for sale or lease on the general market in the form of tangible personal property and sold or leased in the form of tangible personal property are subject to tax irrespective of the fact that the program may require some modification for a purchaser's particular computer. Pre-written or canned computer programs are taxable because the intellectual property contained in the canned program is no different than the intellectual property in a videotape or a textbook.

Sales Tax Information Bulletin 8 (November 2011), 20111228 Ind. Reg. 045110765NRA, now provides that:

Prewritten computer software maintained on computer servers outside of Indiana also is subject to tax when accessed electronically via the Internet (i.e., "cloud computing"). The accessing of prewritten computer software by Indiana residents constitutes a transfer of the software because the customers gain constructive possession and the right to use, control, or direct the use of the software.

Example #3: An Indiana resident purchases a new computer that enables the purchaser to access prewritten computer programs maintained on a third party's computer servers located outside of Indiana. The purchaser never receives the software in a tangible medium. Instead, the purchaser's software, including any documents created with the software, is housed on the third party's server. The sales of these programs are subject to tax.

Taxpayer apparently believes that the 13 programs that it purchased, or purchased access to, represent transactions in which Taxpayer paid for a service and not tangible personal property. During the hearing, Taxpayer provided 9 invoices. However, in many instances, it is unclear on the face of the invoice what exactly Taxpayer purchased.

Following the hearing, the Department asked Taxpayer to provide copies of user agreements, maintenance agreements, or service agreements showing terms of the various software licenses. Taxpayer did not submit documents in response to the Department's request.

As noted above, it is the Taxpayer's responsibility to establish that the proposed tax assessment is incorrect. IC § 6-8.1-5-1(c) states that, "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made."

Based on the information found on the face of each invoice and on the supplemental information provided by Taxpayer during the administrative hearing, the Department is unable to agree that Taxpayer has met its burden of demonstrating that the invoices provided demonstrate that the transaction is not subject to sales or use tax. The invoices are either insufficiently detailed to understand the underlying transaction, or clearly indicate Taxpayer purchased tangible personal property such as pre-written software.

Taxpayer has failed to meet its statutory responsibility of demonstrating that the proposed assessment is incorrect. IC § 6-8.1-5-1(c). Therefore, Taxpayer's protest regarding the assessment of additional use tax is denied.

FINDING

Taxpayer's protest is respectfully denied.

II. Sales and Use Tax – GPS Units.

Taxpayer purchased GPS units that it installed on customer's vehicles it sold as a requirement of financing the vehicle. The purpose of installing the GPS units was for Taxpayer to be able to locate the vehicles if the customer did not follow through with their payments. The audit determined that these GPS units were subject to use tax. Taxpayer maintains that the purchase of GPS units was a sale for resale, since the GPS units were

installed and sold with the car, and therefore not subject to tax.

IC § 6-2.5-5-8(b) provides that:

Transactions involving tangible personal property other than a new motor vehicle are exempt from the state gross retail tax if the person acquiring the property acquires it for resale, rental, or leasing in the ordinary course of the person's business without changing the form of the property.

45 IAC 2.2-5-15 provides further that:

(a) The state gross retail tax shall not apply to sales of any tangible personal property to a purchaser who purchases the same for the purpose of reselling, renting or leasing, in the regular course of the purchaser's business, such tangible personal property in the form in which it is sold to such purchaser.

(b) General rule. Sales of tangible personal property for resale, rental or leasing are exempt from tax if all of the following conditions are satisfied:

(1) The tangible personal property is sold to a purchaser who purchases this property to resell, rent or lease it;

(2) The purchaser is occupationally engaged in reselling, renting or leasing such property in the regular course of his business; and

(3) The property is resold, rented or leased in the same form in which it was purchased.

(c) Application of general rule.

(1) The tangible personal property must be sold to a purchaser who makes the purchase with the intention of reselling, renting or leasing the property. This exemption does not apply to purchasers who intend to consume or use the property or add value to the property through the rendition of services or performance of work with respect to such property.

(2) The purchaser must be occupationally engaged in reselling, renting or leasing such property in the regular course of his business. Occasional sales and sales by servicemen in the course of rendering services shall be conclusive evidence that the purchaser is not occupationally engaged in reselling the purchased property in the regular course of his business.

(3) The property must be resold, rented or leased in the same form in which it was purchased.

The Indiana Tax Court has addressed the "resale exemption" in Brambles Industries, Inc. v. Indiana Dep't of State Revenue, 892 N.E.2d 1287 (Ind. Tax Ct. 2008). In this case, a manufacturer that was seeking the "resale exemption" under IC § 6-2.5-5-8 for pallets by maintaining that "the price of pallet was incorporated into the price of their products" was denied the exemption. The Tax Court explained, as follows:

Indiana Code § 6-2.5-5-8 exempts from tax "[t]ransactions involving tangible personal property ... if the person acquiring the property acquires it for resale, rental, or leasing in the ordinary course of the person's business [.]" Ind. Code Ann. § 6-2.5-5-8(b) (West 2001) (amended 2003). See also 45 Ind. Admin. Code 2.2-5-15(a) (2001). This Court has previously explained that in order to show entitlement to the sale for resale exemption, the taxpayer must demonstrate that it received itemized consideration for the item. See Miles, Inc. v. Indiana Dep't of State Revenue, 659 N.E.2d 1158, 1165 (Ind. Tax Ct.1995) (discount coupons inserted in boxes were not resold because customers did not pay itemized amount for them); Indiana Bell Tel. Co. v. Indiana Dep't of State Revenue, 627 N.E.2d 1386, 1389 (Ind. Tax Ct.1994) (telephone directories, the cost of which was built into customers' monthly bills, were not resold for purposes of the exemption because their cost was not itemized in the bills); USAir, Inc. v. Indiana Dep't of State Revenue, 542 N.E.2d 1033, 1035-36 (Ind. Tax Ct.1989) (holding that meals provided on airline's flights were not resold because there was nothing in the price of the ticket to reflect the price of the food). "Moreover, separate bargaining must occur between the customer and the taxpayer for the exchange of that particular item." Miles, 659 N.E.2d at 1165. See also Greensburg Motel Assocs. v. Indiana Dep't of State Revenue, 629 N.E.2d 1302, 1305-06 (Ind. Tax Ct.1994) (holding that consumable and non-consumable items provided in hotel guest rooms were not resold because the hotel's customers did not bargain for those items).

Brambles, 892 N.E.2d . at 1289-90.

Accordingly, for items to be sold in a retail transaction, the items must be listed separately on the invoices–i.e., the GPS units separate from the vehicle. In the instant case, Taxpayer has not demonstrated that it was selling the GPS units themselves by showing there was itemized consideration for the GPS units, nor has Taxpayer demonstrated that there was separate bargaining for them. After the hearing, the Department requested sample invoices of automobile purchases to customers for whom a GPS unit was included in order to see how the units were being sold to its customers; however, this information was not provided.

The GPS units are also not a material part of the vehicles Taxpayer sells. See Miles, Inc. v. Indiana Dep't of State Revenue, 659 N.E. 2d 1158, 1164 (Ind. Tax Ct. 1995) (explaining that while each chemical or ingredient in the Alka-Seltzer is a "material part" of or essential to the product, the coupons that are inserted into the packaging are not a "material part" of or essential to the product because the coupons do not impact the product's effectiveness and have an undertaking that is vastly different from the products "task of alleviating physical maladies.")

Taxpayer provided no information to show that the GPS units were being resold to their customers, and therefore has not met its burden of proof required under IC § 6-8.1-5-1(c). Based on the above, the purchase and

use of the GPS units does not qualify for exemption from sales or use tax. Since Taxpayer did not pay sales tax at the time of the purchase of the GPS units, use tax is properly imposed.

FINDING

Taxpayer's protest is respectfully denied.

Posted: 01/29/2014 by Legislative Services Agency
An html version of this document.